

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

| | | |
|--------------------------------------|---|-----------------|
| THE APPLICATION OF MILLSTONE WATER |) | |
| COMPANY FOR A RATE ADJUSTMENT |) | CASE NO. 91-254 |
| PURSUANT TO THE ALTERNATIVE RATE |) | |
| FILING PROCEDURE FOR SMALL UTILITIES |) | |

O R D E R

On September 18, 1991, Millstone Water Company ("Millstone") filed its application for Commission approval of a proposed increase in its rates for water service. Commission Staff, having performed a limited financial review of Millstone's operations, has prepared the attached Staff Report containing Staff's findings and recommendations regarding Millstone's proposed rates. All parties should review the report carefully and provide any written comments or requests for a hearing or informal conference no later than 15 days from the date of this Order.

IT IS THEREFORE ORDERED that all parties shall have 15 days from the date of this Order to provide written comments regarding the attached Staff Report or requests for a hearing or informal conference. If no request for a hearing or informal conference is received, then this case will be submitted to the Commission for a decision.

Done at Frankfort, Kentucky this

10th day of February, 1992.

PUBLIC SERVICE COMMISSION


For the Commission

ATTEST:


Executive Director

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF MILLSTONE WATER)
COMPANY FOR A RATE ADJUSTMENT)
PURSUANT TO THE ALTERNATIVE RATE) CASE NO. 91-254
FILING PROCEDURE FOR SMALL UTILITIES)

STAFF REPORT

January 29, 1992

Prepared By: Karen Harrod
Public Utility Financial
Analyst, Chief
Water and Sewer Revenue
Requirements Branch
Rates and Tariffs Division

Prepared By: John Geoghegan
Public Utility Rate
Analyst, Principal
Communications, Water and
Sewer Rate Design Branch
Research Division

STAFF REPORT
ON
MILLSTONE WATER COMPANY
CASE NO. 91-254

A. Preface

On July 29, 1991, Millstone Water Company ("Millstone") submitted an application to the Commission seeking to increase its rates pursuant to the Alternative Rate Filing Procedure for small utilities. The application was considered filed on September 18, 1991 when all deficiencies were cured. The rates proposed by Millstone would generate approximately \$10,800 annually in additional revenues, an increase of 167 percent over normalized test-year operating revenues from water sales of \$6,480.

In order to evaluate the requested increase, the Commission Staff ("Staff") chose to perform a limited financial review of Millstone's operations for the test period, calendar year 1990. Carl Combs of the Commission's Division of Rates and Tariffs attempted to conduct the review on August 13, 1991 at Millstone's office in Leburn, Kentucky. However, no test-year records were available for his review at that time. Subsequently, Mr. Combs resigned from his position with the Commission effective September 15, 1991. As of that date, this case was transferred to Karen Harrod for completion. John Geoghegan, of the Commission's Division of Research, performed his review of Millstone's revenues at the Commission's office in Frankfort, Kentucky.

The findings of Staff's review have been reduced to writing in this report. John Geoghegan is responsible for the sections

relating to operating revenues and rate design. The remaining sections of the Staff Report were prepared by Karen Harrod. Based upon the findings of this report, Staff recommends that Millstone be allowed to increase its annual revenues by \$6,714.

Scope

The scope of the review was limited to obtaining information to determine whether test-period operating revenues and expenses were representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

B. Revenue Requirements Determination

Operating Revenues

Millstone's 45 customers are currently paying \$12 per month for service. This produces \$6,480 in annual revenue for the company. Millstone's proposed rate of \$30 per month would produce \$16,200 in annual revenue.

Operation and Maintenance Expenses

For the test year, Millstone reported operating expenses of \$5,196 which it proposed to increase by \$19,550. The pro forma adjustments to test-period expenses are discussed in the following sections of this report.

It should be noted that the only records available to Staff were cancelled checks for the months of February 1990 through January 1991, and one invoice for chlorine purchased in August 1991. Mr. Combs requested additional information by phone and

Mrs. Harrod requested additional information by letter dated September 23, 1991. No response was filed to either of those requests.

On November 22, 1991, an Informal Conference was held at the Commission's offices in Frankfort, Kentucky. As a result of this conference Mr. B. B. King, the owner of Millstone, provided some additional documentation including a copy of an Agreed Order ("Agreed Order") with the Natural Resources and Environmental Protection Cabinet, dated May 3, 1991, which set forth certain requirements to be met by Millstone.

Salary Expense

Millstone did not report any salary expense for the test year. In its application, an adjustment was proposed to include salary expense of \$15,000 based on Millstone's understanding that "new regulations require personnel on site 24 hours per day." According to Mr. King, the "regulations" referred to are included in the Agreed Order. The Agreed Order required Millstone to obtain the services of a certified drinking water treatment operator by December 1, 1990. During the Informal Conference Mr. King indicated that he agreed to hire an operator at a cost of \$200 per month plus gasoline expenses. The operator would make one trip per week to both Millstone and Haymond Water Company ("Haymond"), another utility owned by Mr. King. Therefore, Staff recommends that 50% of the operator expense of \$2,400 or \$1,200, be allocated to Millstone. Accordingly, an adjustment has been made to include salary expense of \$1,200 for contract labor. The

gasoline expenses will be addressed in the Fuel Power Section of this report.

Chemicals

For the test year, Millstone reported chemicals expense of \$450. An adjustment was proposed to increase this expense to a level of \$4,550 based on purchasing 26 barrels of chlorine at \$175 per barrel. Although a chlorine invoice was provided, it did not reflect a per barrel cost of \$175. In addition, no documentation was submitted to support the need for 26 barrels of chlorine. The Agreed Order requires Millstone to provide continuous, automatic disinfection by chlorination at all times. During the Informal Conference Mr. King indicated that Millstone would require 2-3 drums of chlorine per month at a cost of \$160 per drum. Based on an average of 2.5 drums per month this results in an annual expense of \$4,800, an increase of \$4,350 over the test year level of \$450. Accordingly, Staff recommends an increase to chemicals expense of \$4,350.

Purchased Power

In its application Millstone did not propose an adjustment to test-year purchased power expense. However, during the Informal Conference, Mr. King stated that Millstone's monthly electric bill ranged from \$70-\$80 per month. Based upon Staff's review, the cancelled checks reflect an average monthly expense of \$73.48 for the months of April 1990 - January 1991. Based on this average, annualized purchased power expense would be \$882. Therefore, Staff recommends an increase of \$203 over the test year level of \$679.

Fuel Power Expense

For the test year Millstone reported fuel power expense of \$292. Based on Staff's review, this expense was for the purchase of gas. During the Informal Conference, Mr. King indicated that he would be reimbursing the plant operator for gasoline and that the operator would be required to drive approximately 80 miles per week. Mr. King did not indicate whether gasoline expenses would be reimbursed according to actual cost or on a per mile basis. Therefore, Staff did not have sufficient documentation to calculate an adjustment to test year expense.

Contractual Service Expense

Millstone reported test-year contractual services expense of \$670. Based on Staff's review this expense was for monthly water sampling service performed by Conjun Laboratories, Inc. Millstone filed a letter from Conjun Laboratories, Inc. which stated that Mr. King's total expenses incurred during 1991 were \$1,470. Per a conversation with Janet Madden, a representative of Conjun Laboratories, Inc., this amount included monthly sampling at \$50 per month for Millstone and additional compliance testing for both Millstone and Haymond at a cost of \$870. Staff therefore recommends an increase to test year expense of \$365¹ to reflect Millstone's current level of contractual services expense.

Depreciation Expense

For the test year Millstone reported depreciation expense of \$1,129. Based on Staff's review, \$600 of this expense was the

¹ $(\$50 \times 12) + (\$870 \times .5) = \$1,035 - \$670 = \$365.$

write-off of a pump purchased during the test year. After consulting with the Commission's Engineering Division, Staff is of the opinion that it would be more appropriate to capitalize the expenditure and depreciate it over a period of 5 years, resulting in an annual expense of \$120. Accordingly, Staff recommends a decrease to depreciation expense of \$480.²

In the information filed subsequent to the Informal Conference, Millstone included documentation from Westfall Enterprises, Inc. which listed items that had been purchased by Mr. King for Millstone and Haymond. The listing did not include dates the items were purchased nor did it indicate which utility the items were purchased for. According to Mr. King each of these items were purchased for both Haymond and Millstone. The total amount of pumps, parts, etc. included on the list was \$4,725.08. Staff has decreased this amount by \$845.72 to eliminate expenses for the aforementioned pump and various parts which appear to have been accounted for in test year expenses, based on the review of Millstone's cancelled checks. The remaining pumps and parts have been capitalized and depreciated over a period of 5 years, resulting in an increase to test-year depreciation expense of \$776.³

Based on these adjustments, Staff recommends a net increase to depreciation expense of \$296.

² $\$600 - \$120 = \$480.$

³ $(\$4,725 - \$846) \div 5 = \$776.$

Operations Summary

Based on the recommendations made by Staff, Millstone's operating statement would appear as follows:

| | <u>Test Year Actual</u> | <u>Recommended Adjustments</u> | <u>Test Year Adjusted</u> |
|-------------------------|-----------------------------|------------------------------------|-------------------------------|
| Operating Revenues | \$ 5,571 | \$ 909 | \$ 6,480 |
| Operating Expenses | | | |
| Salary Expense | \$ -0- | \$ 1,200 | \$ 1,200 |
| Purchased Power | 679 | 203 | 882 |
| Fuel Power Production | 292 | -0- | 292 |
| Chemicals | 450 | 4,350 | 4,800 |
| Contractual Services | 670 | 365 | 1,035 |
| Miscellaneous | 1,977 | -0- | 1,977 |
| Depreciation Expense | <u>1,129</u> | <u>296</u> | <u>1,425</u> |
| Total Operating Expense | <u>5,197</u> | <u>6,414</u> | <u>11,611</u> |
| Net Income | <u>\$ 374</u> | <u>\$(5,505)</u> | <u>\$(5,131)</u> |

Revenue Requirements Determination

The approach generally used by this Commission to determine revenue requirements for small, privately-owned utilities is an 88 percent operating ratio. Staff's adjusted operations provide Millstone with an operating ratio of 179⁴ percent. Staff is of the opinion that an 88 percent operating ratio would allow Millstone sufficient revenues to cover its operating expenses and to provide for reasonable equity growth. Based on an operating ratio of 88 percent, Staff has determined Millstone's revenue requirement to be \$13,194.⁵ Therefore, Staff recommends that

⁴ \$11,611 + \$6,480 = 1.79.

⁵ \$11,611 + .88 = \$13,194.

Millstone be allowed to increase its annual operating revenues by \$6,714.⁶

C. Other Issues

Millstone does not maintain adequate bookkeeping records. It is Staff's recommendation that Millstone maintain, at a minimum, a cash receipts and disbursements journal to record all revenues and expenditures of the company. Millstone should also maintain a permanent file of paid invoices. These procedures should be implemented immediately. Adequate record-keeping will prove beneficial to Millstone in routine business transactions and in future rate proceedings with this Commission.

D. Rate Design

Staff recommends that Millstone's current rate design be maintained. The rate recommended by Staff is set out in Appendix A and will generate \$13,203 in annual revenue.

⁶ Revenue Requirement
Less: Normalized Test Year Revenues
Required Increase

\$13,194
6,480
\$ 6,714

E. Signatures



Prepared By: Karen Harrod
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Rates and Tariffs Division



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Public Utility Rate
Analyst, Principal
Communications, Water and
Sewer Rate Design Branch
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APPENDIX A
TO STAFF REPORT CASE NO. 91-254

The Staff recommends the following rate be prescribed for customers of Millstone Water Company.

Monthly Rate

\$24.45